



State of California  
**Franchise Tax Board**

10.18.2007

**FTB NOTICE 2007-4**

**Additional 45-day Extension to File Complete IRS Forms 8886 – FTB Notice 2007-3 Modified**

This Notice modifies FTB Notice 2007-3 by providing taxpayers with an additional 45 days from the due date specified under FTB Notice 2007-3 to file complete IRS Forms 8886 to disclose their participation in reportable transactions before the Franchise Tax Board (FTB) assesses penalties pursuant to Revenue and Taxation Code (RTC) section 19772.

FTB Notice 2007-3 advised taxpayers and practitioners that the FTB was allowing taxpayers who filed incomplete IRS Forms 8886, *Reportable Transaction Disclosure Statement*, or any successor form, or who failed to file a Form 8886 when it was due, a period of 60 days from the date of the Notice (July 31, 2007) to file complete disclosure statements for any transaction that should have been disclosed on or before the date of the Notice. The filing due date under FTB Notice 2007-3 was October 1, 2007. FTB Notice 2007-3 further advised taxpayers that if they failed to meet this deadline, the FTB would assess penalties pursuant to RTC section 19772.

There has been considerable confusion over the filing obligations applicable to certain categories of reportable transactions, in particular the **Transactions with Contractual Protection** category under Treasury Regulation section 1.6011-4(b)(4). In order to address this confusion and to insure that taxpayers are able to comply with their disclosure reporting requirements, the FTB is extending the original filing deadline under FTB Notice 2007-3 to November 15, 2007, for taxpayers to file complete disclosure statements for any transaction that should have been disclosed on or before the date required by FTB Notice 2007-3.

**I. Reportable Transactions**

RTC section 18407 incorporates by reference Internal Revenue Code (IRC) section 6011 and the regulations thereunder. Section 1.6011-4(a) of the Treasury Regulations requires a taxpayer that participates in a reportable transaction, including a listed transaction, to disclose certain information with respect to the reportable transaction. FTB Notice 2007-3 described the disclosure requirements under Treasury Regulation section 1.6011-4, including the requirement to report disclosures to FTB on IRS Form 8886.

Under Treasury Regulation section 1.6011-4(b) there are six categories of reportable transactions:<sup>1</sup>

[1] *Listed Transactions* – A listed transaction is a reportable transaction that is the same as or substantially similar to one of the types of transactions that the IRS has determined to be a tax avoidance transaction. These transactions are identified by notice, regulation or other form of published guidance as a listed transaction. (Treas. Reg. § 1.6011-4(b)(2).)

[2] *Confidential Transactions* – A confidential transaction is a transaction that is offered to a taxpayer under conditions of confidentiality to protect the tax advisor's strategy and for which the taxpayer paid an advisor a minimum fee. (Treas. Reg. § 1.6011-4(b)(3).)

[3] *Loss Transactions* – This category of reportable transactions includes a transaction that results in a taxpayer claiming a loss under IRC section 165 that exceeds certain thresholds. (Treas. Reg. § 1.6011-4(b)(5).)

[4] *Transactions with a Significant Book-Tax Difference* – A transaction with a significant book-tax difference is a transaction where the amount for tax purposes of any item or items of income, gain, expense, or loss from the transaction differs by more than \$10 million on a gross basis from the amount of the item or items for book purposes in any taxable year. (Treas. Reg. § 1.6011-4(b)(6).)<sup>2</sup>

[5] *Transactions Involving a Brief Asset Holding Period* – A transaction involving a brief asset holding period is any transaction where a taxpayer claims a tax credit of more than \$250,000 if the asset giving rise to the credit was held by the taxpayer for 45 days or less. (Treas. Reg. § 1.6011-4(b)(7).)<sup>3</sup>

[6] The final category of reportable transactions is **Transactions with Contractual Protection**. (Treas. Reg. § 1.6011-4(b)(4).) It is this category of reportable transactions that has caused significant confusion for taxpayers in determining whether they have a disclosure requirement under the law to which they must respond by filing under FTB Notice 2007-3.

Generally, a transaction with contractual protection is any transaction for which the taxpayer or related party (as described in IRC sections 267(b) or 707(b)) has a right to a full or partial refund of fees paid if all or a part of the intended tax consequences from the transaction are not sustained. It also includes a transaction for which fees are contingent upon the taxpayer's realization of tax benefits from the transaction. These provisions only apply with respect to fees paid by or on behalf of a taxpayer or a related party to any person who makes

---

<sup>1</sup> These are the categories of reportable transactions that applied to transactions entered into before January 6, 2006. Taxpayers that had a disclosure requirement for the period that these categories existed and failed to disclose will be subject to the penalty under RTC section 19772 unless they file required disclosure statements by November 15, 2007.

<sup>2</sup> In IRS Notice 2006-6, the Internal Revenue Service (IRS) announced that taxpayers were no longer required to disclose the significant book-tax difference category of reportable transactions, unless the transaction met one of the other five categories of reportable transactions. This Notice was effective for transactions with a significant book-tax difference that would otherwise have to be disclosed on or after January 6, 2006. California is following IRS Notice 2006-6. In final regulations, effective August 3, 2007, the IRS eliminated the transactions with a significant book-tax difference category of reportable transactions and replaced it with a "transactions of interest" category of reportable transactions that applies to transactions entered into after November 1, 2006.

<sup>3</sup> In those same final regulations, the IRS eliminated the brief asset holding period reportable transaction category.

or provides a statement, oral or written, to the taxpayer or related party as to the potential tax consequences that may result from the transaction.

This category does not include "previously reported transactions." (See Treas. Reg. § 1.6011-4(b)(4)(iii)(B).) If a person makes or provides a statement to a taxpayer as to the potential tax consequences that may result from a transaction only after the taxpayer has entered into the transaction and reported the consequences of the transaction on a filed tax return, and the person has not previously received fees from the taxpayer relating to the transaction, then any refundable or contingent fees paid by the taxpayer to the person that made or provided that statement are not taken into account in determining whether the transaction has contractual protection.

Generally, if a taxpayer receives advice after entering into a transaction and filing an original return that reflects the consequences of the transaction, where the fees relating to that advice are contingent upon the taxpayer realizing certain tax benefits resulting from that advice by filing an amended return, and the advisor has not previously advised the taxpayer and not received fees from the taxpayer with respect to that transaction, then consistent with the previously reported transaction exception under Treasury Regulation section 1.6011-4(b)(4)(iii)(B), the taxpayer has not participated in a transaction with contractual protection and the transaction is not reportable. However, the transaction may still be reportable if one of the other categories of reportable transactions under Treasury Regulation section 1.6011-4(b) applies.

For example, a taxpayer files an original return reflecting a wage expense. After the return has been filed, the taxpayer receives advice from a new advisor that the expenditure qualifies for a California-only enterprise zone credit and files an amended return claiming the credit. Even if the taxpayer has a right to a full or partial refund of fees paid for the advice in the event the tax treatment is not sustained or if the fees are contingent on the taxpayer's realization of the credit for the expenditure, the taxpayer has not participated in a reportable transaction under Treasury Regulation section 1.6011-4(b)(4).

If, however, a taxpayer receives advice prior to filing an original return and the taxpayer has a right to a full or partial refund of fees paid in the event the tax treatment is not sustained or if the fees are contingent as described under Treasury Regulation section 1.6011-4(b)(4)(i), then, even if the tax treatment based on that advice is only reflected on an amended return, the transaction may not be considered a previously reported transaction as described in Treasury Regulation section 1.6011-4(b)(4)(iii)(B).

Taxpayers should analyze all the facts and circumstances relating to their transaction to determine if they have a reportable transaction subject to disclosure under any of the reportable transaction categories identified above, including a transaction with contractual protections where the taxpayer has a fee arrangement as described above with any person who has made or provided a written or oral statement to the taxpayer or related party as to the potential tax consequences that may result from the transaction. (See Treas. Reg. § 1.6011-4(b)(4)(ii).)<sup>4</sup>

---

<sup>4</sup> The FTB is considering but has not yet determined whether to identify transactions exempt from the disclosure requirements, similar to what the IRS has done with IRS Rev. Proc. 2007-20.

## II. Filing Instructions

A taxpayer filing a disclosure statement in accordance with this Notice need only file the statement with the FTB Abusive Tax Shelter Unit (ATSU) and need not file an amended return to satisfy the disclosure requirements.<sup>5</sup> For disclosure statements being filed in response to this Notice, Taxpayers should write in red on the top of the Form 8886 **"FTB Notice 2007-3."**

Mail the Form 8886 to FTB's ATSU at the following address:

US Mail:  
ATSU 398 MS: F385  
FRANCHISE TAX BOARD  
P.O. BOX 1673  
SACRAMENTO, CA 95812-9900

For Courier Service Delivery or Private Courier Mail:

ATSU 398 MS: F385  
FRANCHISE TAX BOARD  
SACRAMENTO, CA 95827-9900

The principal author of this notice is Craig Scott of the Franchise Tax Board, Legal Division. For further information regarding this notice, contact Mr. Scott at the Franchise Tax Board, Legal Division, P. O. Box 1720, Rancho Cordova, CA 95741-1720.

---

<sup>5</sup> Taxpayers with closed audits or with open audits that have transactions that should have been disclosed under Treasury Regulation section 1.6011-4 are not exempt from the disclosure requirements. Participants in the FTB's 2004 Voluntary Compliance Initiative (RTC section 19751 et seq.) and in the 2006 California Tax Shelter Resolution Initiative (FTB Notice 2006-1) are not subject to penalties under RTC section 19772 for transactions disclosed under these initiatives.